

Letter of Findings Number: 07-0032 & 07-0033
Sales and Use Tax
For Tax Years 2003-2005

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ISSUES

I. Sales and Use Tax—Imposition.

Authority: IC § 6-2.5-1-1; IC § 6-2.5-1-2; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-4-1; IC § 6-8.1-5-1; IC § 6-8.1-5-4; [45 IAC 2.2-1-1](#); [45 IAC 2.2-4-1](#); *Frame Station, Inc. v. Indiana Dep't of Revenue*, 771 N.E.2d 129 (Ind. Tax Ct. 2002).

Taxpayer protests the imposition of use tax on a variety of purchases.

II. Tax Administration—Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer provides auto repair services, operates an auto racing team, and sells recreational vehicles ("RV") in Indiana. After an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer owed additional use tax and assessed a negligence penalty for the 2003-2005 tax years. The Department found that Taxpayer made a variety of purchases without paying sales tax at the time of purchase or remitting use tax to the Department. Taxpayer protests the assessment of tax and penalty. An administrative hearing was held, and this Letter of Findings results. Further facts will be supplied as required.

I. Sales and Use Tax—Imposition.

DISCUSSION

Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that an assessment is incorrect.

IC § 6-2.5-2-1 provides:

- (a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.
- (b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

IC § 6-2.5-3-2(a) provides:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Accordingly, Indiana imposes a sales tax on retail transactions and a complementary use tax on tangible personal property that is stored, used, or consumed in the state. IC § 6-2.5-1-1 et seq. An exemption from the use tax is granted for transactions where the gross retail tax ("sales tax") was paid at the time of purchase pursuant to IC § 6-2.5-3-4. Since Taxpayer failed to pay sales tax at the time of purchase, the Department found that the purchases were subject to use tax.

A. Vehicle Parts.

Taxpayer protests the imposition of use tax on its purchase and use of the vehicle parts for two reasons. First, Taxpayer asserts that the parts are used by its repair shop to repair vehicles for its auto dealership, and when its repair shop bills the auto dealership for the repairs the repair shop includes a charge for tax on the parts used to repair the dealership's vehicles. However, Taxpayer has failed to provide sufficient documentation to demonstrate that the parts listed in the audit were billed to the dealership or that tax was collected.

Second, Taxpayer asserts that even if tax was not collected on the transfer of the parts to the dealership since the dealership collected sales tax from the purchaser of the vehicle and the purchase price included the cost of repairs, sales tax was collected for the transfer of the vehicle parts. However, Taxpayer's assertion ignores the fact that two separate transactions take place each of which is a transaction that is subject to sales or use tax. Specifically, Taxpayer's retail shop incurred its sales and use tax liability at the time of purchase and use of the vehicle parts, and the dealership's customer's subsequent payment of sales tax on its purchase of the vehicle does not discharge Taxpayer's liability for Taxpayer's transaction.

Therefore, Taxpayer's protest is respectfully denied.

B. Mail Service Reminders.

Taxpayer protests the imposition of use tax on its purchase and use of "mail service reminders." Taxpayer

purchases mail service reminders that are printed and mailed to its customers by the printing company. Taxpayer maintains that the Department has assessed use tax on services, which are exempt from sales and use tax.

As stated previously, Indiana imposes a sales tax on retail transactions and a complementary use tax on tangible personal property that is stored, used, or consumed in the state. IC § 6-2.5-1-1 et seq. A retail transaction is the transfer, in the ordinary course of business, of tangible personal property for consideration. IC § 6-2.5-4-1(b). Except for certain enumerated services, sales of services are generally not retail transactions and are not subject to sales or use tax.

However, services that are performed as part of a retail "unitary transaction" are subject to sales and use tax. IC § 6-2.5-1-2(b). A retail "unitary transaction" is one in which items of personal property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC § 6-2.5-1-1(a). A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. [45 IAC 2.2-1-1\(a\)](#).

During the course of protest, Taxpayer produced a sample invoice demonstrating the manner in which it was billed. The evidence presented by Taxpayer demonstrates that Taxpayer's invoices do represent unitary transactions which would subject the entire amount to use tax.

Therefore, Taxpayer's protest is denied.

C. "Subcontracted Labor."

Taxpayer protests the imposition of use tax on its purchase and use of "solvent cleaner," "awnings," a "CO2 bottle 10oz-crome," "cage window attachments," and a "hardware upgrade." Taxpayer asserts that the purchases were for "subcontracted labor," which is the equivalent to services and is exempt from sales and use tax.

1. "Solvent Cleaner."

During the course of the protest, Taxpayer submitted a sample invoice demonstrating the manner in which it was billed for the "solvent cleaner." However, the evidence presented by Taxpayer demonstrates that Taxpayer's invoice represents charges for the "solvent cleaner" chemicals, which would be subject to use tax.

Therefore, Taxpayer's protest is denied.

2. "Awnings."

Taxpayer has not provided any documentation to support its assertion that the purchases of "awnings" represent payment for the provision of services.

IC § 6-8.1-5-4(a) provides:

Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.

Accordingly, it is Taxpayer's responsibility to retain the documentation that supports the amounts it used to determine the tax owed. Moreover, Taxpayer did not cite any statute, regulation, or case law for the proposition that the Department is required to accept Taxpayer's assertions as to the nature of these transactions without providing the supporting documentation. Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that an assessment is incorrect. Since Taxpayer failed to produce any documentation that demonstrates that the Department's assessment was incorrect, then Taxpayer has failed to meet its burden of proof.

Therefore, Taxpayer's protest is denied.

3. "CO2 Bottle 10oz-Crome."

During the course of the protest, Taxpayer submitted a sample invoice demonstrating the manner in which it was billed for a "CO2 Bottle 10oz-Crome." However, the evidence presented by Taxpayer demonstrates that the charge on Taxpayer's invoice represents a charge for a 10 ounce bottle of chrome, which would be subject to use tax.

Therefore, Taxpayer's protest is denied.

4. "Cage Window Attachments."

During the course of protest, Taxpayer produced an invoice demonstrating the manner in which it was billed for the "cage window attachments." However, the evidence presented by Taxpayer demonstrates that Taxpayer's invoice represented a unitary transaction, which would subject the entire amount to use tax.

As stated previously, services that are performed as part of a retail "unitary transaction" are subject to sales and use tax. IC § 6-2.5-1-2(b). A retail "unitary transaction" is one in which items of personal property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC § 6-2.5-1-1(a). A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. [45 IAC 2.2-1-1\(a\)](#).

Since the "cage window attachments" were purchased as part of a "unitary transaction," the entire invoice is subject to tax.

Therefore, Taxpayer's protest is denied.

5. Hardware Upgrades.

During the course of the protest, Taxpayer submitted a sample invoice demonstrating the manner in which it was billed for "hardware upgrades." However, the evidence presented by Taxpayer demonstrates that the charges on Taxpayer's invoice represents charges for hardware that upgrades its server, which would be subject to use tax.

Therefore, Taxpayer's protest is denied.

D. RVs.

Taxpayer protests the imposition of use tax on its purchase and use of three RVs. Taxpayer drives RVs that have Taxpayer's RV dealer plates on them to race sites and stays in them overnight. Taxpayer asserts that it did not purchase the RVs, but was using them as "demos" in the capacity of a full-time sales person for another RV dealer.

During the course of protest, Taxpayer submitted various pictures of RVs and a RV sales brochure. However, the documents submitted were insufficient to prove that Taxpayer did not purchase and use the RVs.

IC § 6-8.1-5-4(a) provides:

Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.

Accordingly, it is Taxpayer's responsibility to retain the documentation that supports the amounts it used to determine the tax owed. Moreover, Taxpayer did not cite any statute, regulation, or case law for the proposition that the Department is required to accept Taxpayer's assertions as to the nature of these transactions without providing the supporting documentation. Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that an assessment is incorrect. Since Taxpayer failed to produce any documentation that demonstrates that the Department's assessment was incorrect, then Taxpayer has failed to meet its burden of proof.

Therefore, Taxpayer's protest is denied.

E. Diesel Fuel.

Taxpayer protests the imposition of use tax on its purchase and use of diesel fuel. Taxpayer asserts that sales tax was collected at the time of purchase because the sales tax is included in the price of the diesel.

During the course of the protest, Taxpayer submitted sample invoices demonstrating the manner in which it was billed. However, the evidence presented by Taxpayer is irrelevant because it is not for the audit period and fails to show that tax was paid at the time of purchase. Therefore, Taxpayer failed to provide any documentation to support its assertion that the tax was collected at the time of purchase.

IC § 6-8.1-5-4(a) provides:

Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.

Accordingly, it is Taxpayer's responsibility to retain the documentation that supports the amounts it used to determine the tax owed. Moreover, Taxpayer did not cite any statute, regulation, or case law for the proposition that the Department is required to accept Taxpayer's assertions as to the nature of these transactions without providing the supporting documentation. Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that an assessment is incorrect. Since Taxpayer failed to produce any documentation that demonstrates that the Department's assessment was incorrect, then Taxpayer has failed to meet its burden of proof.

Therefore, Taxpayer's protest is denied.

F. Roller.

Taxpayer protests the imposition of use tax on its purchase and use of a roller. Taxpayer asserts that the Department incorrectly assessed tax on the roller because the audit report listed the purchase price as \$2,512.00 instead of \$25.12. Taxpayer has provided sufficient information to demonstrate that the roller, found on page four of report control number 306277-05, was purchased for \$25.12.

Therefore, Taxpayer's protest is sustained.

G. Gloves.

Taxpayer protests the imposition of use tax on its purchase and use of gloves. Taxpayer asserts that the Department incorrectly assessed use tax on the gloves because the gloves were purchased to be resold to its employees.

During the course of the protest, Taxpayer submitted sample invoices demonstrating the manner in which it billed employees for the gloves. However, the evidence and analysis presented by Taxpayer was insufficient to demonstrate that Taxpayer's invoice represents charges for gloves on which use tax had been assessed.

Therefore, Taxpayer's protest is denied.

H. T-shirt Giveaways.

Taxpayer protests the imposition of use tax on its entire purchase and use of custom designed "T-shirt giveaways." Taxpayer maintains that the amounts listed separately on the T-shirt invoice for designing, bagging, and shipping, and the T-shirts were for the provision of exempt services.

Taxpayer asserts that since the T-shirt printer had separately broken out the labor and materials costs, Taxpayer is not required to pay use tax on the labor charges.

As stated previously, Indiana imposes a sales tax on retail transactions and a complimentary use tax on tangible personal property that is stored, used, or consumed in the state. IC § 6-2.5-1-1 et seq. A retail transaction is defined as occurring when a person "acquires tangible personal property... and transfers that property to another person for consideration." IC § 6-2.5-4-1(b)(1)-(2). Pursuant to IC § 6-2.5-4-1(e) the amount of the retail transaction that is subject to sales and use tax includes "the price of the property transferred" and "any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records." Further, [45 IAC 2.2-4-1\(b\)\(3\)](#) provides that amount of the retail transaction that is subject to tax includes the amounts collected for "services performed or work done on behalf of the seller prior to transfer of such property at retail."

Additionally, in *Frame Station, Inc. v. Indiana Dep't of Revenue*, 771 N.E.2d 129 (Ind. Tax Ct. 2002), the court held that when customers were charged separate amounts for labor and materials for custom framing services the labor charges were subject to sales tax. *Id.* at 131. In arriving at that decision, the court reasoned that the focus of analysis should be "whether [Taxpayers'] services were performed before or after it transferred property to its customers." *Id.* The court found that services that are performed prior to the transfer of the property are taxable, and services that are performed after the transfer of the property are taxable to the extent that the services represent a "unitary transaction" and are "inextricable and indivisible" from the property being transferred. *Id.*

Accordingly, the determinative fact is when the services were performed by the custom T-shirt designer. Since the T-shirt designer's services in designing, bagging, and shipping the T-shirts occur prior to the transfer of the completed T-shirts to the Taxpayer, the services are subject to sales and use tax. The fact that the services are listed separately on the customers' invoices for the completed T-shirts is not relevant.

Therefore, Taxpayer's protest is denied.

FINDING

In summary, Taxpayer's protest of subpart F is sustained, and Taxpayer's protest of subparts A, B, C, D, E, G, and H are denied.

II. Tax Administration—Negligence Penalty.

DISCUSSION

Taxpayer protests the imposition of the ten percent negligence penalty for the tax years in question. The Department refers to IC § 6-8.1-10-2.1(a)(3), which provides, "if a person... incurs, upon examination by the department, a deficiency that is due to negligence... the person is subject to a penalty."

[45 IAC 15-11-2\(b\)](#) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at [45 IAC 15-11-2\(c\)](#) as follows:

The department shall waive the negligence penalty imposed under IC § 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

In this case, Taxpayer incurred a deficiency which the Department determined was due to negligence under [45 IAC 15-11-2\(b\)](#), and so was subject to a penalty under IC § 6-8.1-10-2.1(a). Despite the fact that Taxpayer stated that it has recently hired a new accounting firm, Taxpayer has not provided sufficient information to establish that this event, occurring after the fact, is relevant to the tax deficiencies for the tax periods at issue. In addition, while Taxpayer has established that it does not owe some of the proposed assessments, Taxpayer has not affirmatively established that its failure to pay the remaining deficiencies was due to reasonable cause and not due to negligence, as required by [45 IAC 15-11-2\(c\)](#).

FINDING

Taxpayer's protest to the imposition of penalty is denied.

